BEFORE THE UNITED STATES DEPARTMENT OF AGRICULTURE AGRICULTURAL MARKETING SERVICE

In the Matter of	**:**	**Docket Nos.:**
	:	
Milk In The Mideast	**:**	**AO- 166-A72;**
	:	
Marketing Area	**:**	**DA-05-01**

POST-HEARING BRIEF ON BEHALF OF DAIRY FARMERS OF AMERICA, INC. (DFA), MICHIGAN MILK PRODUCERS ASSOCIATION, INC., (MMPA), NATIONAL FARMERS ORGANIZATION, INC. (NFO), DAIRYLEA COOPERATIVE INC. (DAIRYLEA) AND LAND O'LAKES, INC. (LOL)

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I. INTRODUCTION

This brief is submitted on behalf of Dairy Farmers of America, Inc. ("DFA"); Michigan Milk Producers Association, Inc. ("MMPA"); National Farmers' Organization Inc. ("NFO"); Dairylea Cooperative Inc. ("Dairylea"); and Land O'Lakes Inc. ("LOL"). It addresses all propos ls at the hearing, those advanced by the parties submitting this brief and those proposals submitted or advocated by other participants. The hearing proposals concern (1) appropriate pooling standards for Order 33, including the potential dual pooling of milk; (2) depooling and repooling of milk; and (3) transportation credits for movement of milk to Class I plants. In addition consideration needs to be given to addressing the issues on an expedited basis, without a recommended decision.

There was a consensus among active market participants that Order 33 as presently operating allows disorderly conditions, particularly the pooling of milk without sufficient performance or the depooling and repooling of milk or both. We will discuss these issues and proposals after first describing the market as documented in the hearing record.

II. FACTUAL BACKGROUND

Proponents

1. Dairy Farmers of America, Inc., (DFA) is a Capper-Volstead cooperative association of 13,500 dairy farms producing milk in forty-nine (49) states. DFA regularly markets milk on 9 of the 10 federal milk orders, including Order 33. DFA's Mideast Area Council consists of some 2500 member farms primarily in the marketing area for Order 33. (Tr. 206, 483)

2. Michigan Milk Producers Association, Inc. (MMPA) is a member-owned Capper-Volstead Cooperative of 1680 farms, producing milk in four states. MMPA pools milk on the Mideast Federal Order. (Tr. 206)

3. National Farmers Organization, Inc., (NFO) is a member-owned Capper Volstead association marketing milk for more than 1500 dairy farms in 18 states. NFO pools milk on 6 of the 10 Federal Milk marketing Orders, including the Mideast Federal Order. (Tr. 206)

4. Dairylea Cooperative Inc. (Dairylea) is a member-owned Capper-Volstead cooperative of 2400 member farms producing milk in seven states. Dairylea member milk is pooled in 3 of the 10 Federal Milk Marketing Orders, including the Mideast Order. (Tr. 206)

5. Land O' Lakes, Inc. (LOL) is a national, member-owned Capper-Volstead cooperative, headquartered in Arden Hills, Minnesota, which has member dairy farms and pools milk in the Mideast Federal Order.

Other market and hearing participants

6. Dean Foods Corporation is a national milk and dairy products processor and marketer with 12 fluid milk plants fully regulated in Order 33. (Kinser, Exh. 33)

7. White Eagle Milk Marketing Federation consists of four named member dairy cooperatives (White Eagle Cooperative Association, Alto Dairy, Scioto Cooperative, Erie Cooperative Association) and an unidentified number of unidentified cooperative members. It pools milk for non-member dairy farmers, as well as for its members. White Eagle is managed by Dairy Support, Inc., a wholly owned subsidiary of T.C. Jacoby & Sons, Inc., a proprietary milk merchant and brokerage firm. White Eagle pools about 150 million pounds of milk on Order 33 per month from dairy farms in Ohio, Indiana, Michigan, Wisconsin, and elsewhere. (Leeman Tr. 668–671)

8. Prairie Farms Cooperative is a producer-owned, Capper-Volstead cooperative headquartered in Carlinville, Illinois with distributing plants in Order 33. Through outright ownership and joint venture, it operates 31 milk and dairy processing plants located in nine states. Four of those plants are located in the Order 33 marketing area. (Tr. 491)

9. Foremost Foods USA is a Wisconsin-based Capper-Volstead cooperative which pools and markets milk in Order 33. Foremost has 538 member farms in the Order 33 marketing area. (Tr. 622)

10. Continental Dairy Products is a small cooperative with 21 members which are large dairy farms in the states of Michigan, Indiana, and Ohio. Some of the production of Continental's members is pooled on Order 33, as well as on Orders 5 and 7. (Tr. 442)

11. Independent proprietary handlers, including Superior Dairy, Inc. and United Dairy, Inc., (with plants at Uniontown, PA, Martins Ferry, Ohio, and Charlestown, West Virginia) both represented at this hearing by the White Eagle witness (Tr. 668), Smith Dairy, Arps Dairy, Eastside Jersey, Kroger – Indianapolis, Pleasant View Dairy, Carl Colteryahn, Marburger Dairy, Schneider's Dairy, and Turner's Dairy are fully regulated distributing plants in the Pennsylvania, Ohio, Indiana segment of Order 33, not affiliated with Dean Foods, or fully supplied by DFA. (Gallagher, Tr. 542–546) There are additional proprietary plants in Michigan with the same characteristics. These plants establish the broad diversity of suppliers and customers in Order 33.

12. Independent dairy farmers, not members of any cooperative association for milk marketing purposes, numbering approximately 3000, represent at least 30% of the milk supply in Order 33. Many of these producers are dedicated suppliers to nearby Order 33 distributing plants, including Larry Baer of Marshallville, Ohio, a witness at the hearing. (Tr. 1051–55)

The Market

13. The Mideast Marketing Area, Order 33, reaches from Indiana in the west to West Central Pennsylvania in the east; and from the Upper Peninsula of Michigan in the north to central Kentucky in the south. Among the 10 current federal orders, its Class I volume is the second highest at 6.5 billion pounds of annual Class I sales (Exh. 15, Table 1), reflecting more than 7 billion pounds of Class I disposition at pool plants. (Exh. 6, Table 9)

13a. The Class I sales originate from more than 40 pool distributing plants (Exh. 6, Table 1). The Class I sales from those pool distributing plants are shared by the nearly 10,000 producers in the pool (Exh. 6, Table 15) from 12 states (Exh. 6, Table 17).

14. The pooling of milk from areas not closely associated with the marketing area and without adequate performance for the Class I market has resulted in a reduction in the Order's blend price (or PPD) for the producers who regularly service the Class I market. (Exh. 7, Request 2)

15. The pooling of milk without substantial performance has been facilitated by pooling provisions which allow milk to be pooled on the Order with the requirement of few if any deliveries to distributing plants serving the marketing area.

16. In the fall of 2004, in the months of highest demand for Class I sales, August to November, the percentage of milk pooled on Order 33 from Minnesota, Iowa, Wisconsin, and Illinois, and delivered to distributing plants peaked at 12.4 % in September and was between 6% and 7% for the other fall months. (Exh. 7, Request 3) During those months, the utilization of the market was 35% to 42%. (Exh. 6, Table 7)

17. The estimated impact of distant milk on Order 33 during certain months in 2003 and 2004 was as great as a reduction of $.40 per cwt, in July 2004, on the PPD. (Exh. 7, request

2)

18. In addition to its limited service of Class I markets, milk which is dedicated to manufacturing uses has freely moved on and off the Order to take advantage of price fluctuations and class price inversions. This "open depooling" is a major source of marketing disorder in Order 33.

19. The testimony of dairy producers strongly attested to the disorder from current Order 33 provisions:

a. Bruce Bloom, who operates a third generation dairy farm in Coldwater Michigan with his brother milking 480 cows and serves on the board of the North Central Cooperative, testified regarding the effects of depooling on his family operation. The Blooms suffered negative producer price differentials in 2004 of $3.98 in April, $1.84 in May, and $0.65 in December. According to information from the Market Administrator, depooling was responsible for $1.66, $0.74 and $0.29 of these losses, respectively, amounting to losses of over $16,000 for April, over $7,400 for May and $2,900 for December for the Blooms' farm. (Tr. 369-370)

b. Connie Finton, who serves as Chairman of the Ohio Dairy Industry Forum and Vice Chair of the Ohio Dairy Producers, Incorporated, owns and operates with her husband a dairy farm near New Philadelphia, Ohio, with approximately 70 cows milking year round and supplying Order 33 market at all times. She asserts that depooling negatively impacts the economics of the market area and ultimately leads to the demise of dairy producers in the area. Mrs. Finton stresses the need for prompt action by the Department. (Tr. 449-450)

c. Bill Ramsey and his family farm near Louisville, Ohio. He is part owner and operator of Paradise Valley Farms, Incorporated which is worked by three generations of family

members and four full time employees. He estimates that his dollar losses for April, May and December of 2004 totaled $24,402. Mr. Ramsey is concerned that a significant amount of distant milk is pooled on Order 33 market, but very little of it is actually delivered into the market. The Order rules should reflect economic reality, both for the local producers and those from other Orders. Action by the Secretary should be taken with utmost urgency. (Tr. 452-455)

d. John R. Hathaway milks approximately 40 cows and works as a part time construction worker. His farm is located near Greenville, Ohio. His view is that the current rules on depooling need revision so that the distribution of the proceeds of the sale of milk is equitable in times of volatile milk prices. The current regulations continue to affect his farm's daily operation and he urges the Secretary to act with the utmost urgency to adopt Proposals 1, 2, 7, and 9. (Tr. 459 – 464)

e. Chester Stoll's family farm is located near Marshallville, Ohio and is worked by family and two full time and two part time employees. He serves on the State Board of Ohio NFO and is Ohio NFO's Vice President. Mr. Stoll supports Federal Milk Orders. He is opposed to the practice whereby "paper milk" under the current regulations can draw money out of the hands of farmers who regularly supply the market in Order 33. He sees the current Order as not working to advance the goals of Federal Orders and in need of modification to correct the problem of pooling, depooling and pool riding. He supports the proposals offered by DFA and urges that action be taken in a very timely manner. (Tr. 465 – 470)

f. Tommy R. Croner and his son operate a family owned dairy and potato farm in Berlin, Pennsylvania with 250 cows milking and 45 acres of potatoes under cultivation. He has served on the Corporate Board of Directors of DFA since its inception and serves as the Secretary/Treasurer and Chairman of the Mideast Area Council of DFA. He testified on behalf

of 2,500 DFA members of Federal Order 33. Mr. Croner believes that when depooling occurs it creates an unequal distribution of market proceeds. This unequal distribution of proceeds in turn undermines Federal Order objectives allowing one classification of end use to take advantage of the system by having actual knowledge of prices. He supports Proposals 1, 2, 7 and 9. (Tr. 478 – 483)

g. Brian Wolfe appeared to testify as a representative of Ohio Farmers Union which believes that opportunistic transfers of milk into Order 33 have not happened as a result of local milk shortages, but solely due to the desire of milk handlers to capitalize on excessively volatile and inappropriate class pricing variations, coupled with lax pool qualification criteria. Ohio Farmers Union strongly supports changes in Order 33 to raise requirements for qualifying milk not customarily associated with the Order for inclusion in the pool in any given month. Mr. Wolfe is also Chairman of the Dairy Committee of Ohio. (Tr. 171 – 174)

h. Earl Stitzlein and his son operate an 80-cow dairy and farm 450 acres in Holmes County, Ohio. He is the President of the Independent Milk Producers Association Board, a local co-op that markets its members milk through DMS. Like other small dairy farmers, he is concerned about the negative effect of depooling and repooling on PPD and the impact thereof on his association members and himself. He, on behalf of the Independent Milk Producers Association Board, supports adoption of the proposals put forth by DFA. (Tr. 473-476)

i. Charles Lausin is part of a fifth generation family farm in Geauga County, Ohio with 145 cows milking. He is a member of the Ohio Farm Bureau Board of Directors (OFBB) and the Chairman of its Dairy Advisory Committee. The OFBB is concerned about the negative effect of depooling on PPD and actions that will continue to result in escalating

producer pay price volatility leading to decreased confidence in the Mideast Federal Order. Depooling of milk allows certain milk producers to retain a much larger share of Class III milk proceeds and causes those producers who can not depool to bear the larger cost. According to an Ohio State University Extension State Specialist of Dairy Markets and Policy, 1.87 billion pounds of milk were taken out of the Order in April 2003 costing pool producers $7.4 million; and 1.3 billion pounds in April and May 2004 costing pool producers an estimated $21.3 million. Mr. Lausin advocates two basic changes to the Order. The first and foremost is amending the order to make it more difficult to depool and then reenter the market pool. Secondly, he believes that extensive modifications need to be made to the pricing rules in the Order. (Tr. 375-381)

j. Paul Rohrer and his wife own and operate a dairy farm in Orville, Ohio as the fifth and sixth generations farming their land over a span on 140 years. The Rohrer farm lost $6,000 in the months of April and May 2004. Mr. Rohrer calculates that the annual average negative effect on PPD of $0.36 reported by Cameron Thraen resulted in a $16,000 loss to his farm in 2004. He asks the Secretary to protect producers in the Order from milk entering the order that is not sustained in the market and from voluntary depooling. Mr. Rohrer calls for action by the Secretary on an emergency basis to remedy the depooling situation in Order 33. (Tr. 392 – 394)

20. In addition to the testimony from dairy producers, the testimony from expert witnesses and others from both cooperatives and proprietary plants recognized open depooling as a disorderly marketing condition which should be addressed, although there was not unanimity about the best mechanism for addressing the problem. (Kinser Tr. 949–960; Christ, Tr. 1064–84; Gallagher; Exh. 14, at 26–27; Speck, Tr. 437–39)

21. Allowing producers to jump in and out of the pool freely is unfair to the dedicated

suppliers of the Order 33 Class I market, including the members of the cooperatives submitting this brief. (Tr. 172–74, 371–72, 376–81, 447–49, 453–55, 461–64, 467–68, 473–75, 479–82, 392–94)

22. Distributing plants in Order 33 are generally located further from areas of milk production than are manufacturing plants. There are several areas of substantial distributing plant demand in Order 33 which require milk to be transported substantially greater average distances than milk that is delivered to manufacturing plants. (Exh. 7, Request 7, Request 8)

23. The zone structure of milk prices in Order 33 is not sufficient to defray the additional cost of transporting milk to Class I plants. As a consequence, the suppliers of Class I plants, particularly those suppliers who assure the full balance of a plant's supply needs, are at a competitive disadvantage with producers who dedicate their supply to manufacturing uses.

The Proposals relating to performance requirements (Proposals 1, 2, and 3)

24. Proposals 1, 2, and 3 can be summarized as follows: (1) Proposal 1 would prohibit the possibility of milk being pooled on Order 33 at the same time it is pooled on another marketwide pools, such as the state order pool in California. (2) Proposal 2 would enhance the performance standards for all milk in the Order 33 pool by (a) increasing the monthly deliveries to distributing plants required of pool supply plants by 10 % in each month to 40%; (b) increasing the deliveries to distributing plants required of cooperative supply plants to 40 % in the months of August through November; (c) increasing the required deliveries to distributing plants from Section 7(e) supply plants to 45% in the months of August through November and 35% during the months of December to July; and (d) reducing the proportion of producer milk which can be diverted to nonpool plants by 10% each month to limits of 50% during August through February and 60% during March through July. Its goal is to more fairly define the milk

that should share in the pool's Class I returns.

25. Proposal 3, advanced by Dean Foods Corporation, which would have increased the required days for pool producers to "touch base" was withdrawn at the hearing.

The Proposals relating to open depooling (Proposals 4, 5 ,6 ,7, and 8)

26. The depooling problem was addressed in Proposals 4, 5, 6, 7, and 8. Depooling is a serious marketing problem because it results in different returns from the Order for milk sales; and different pay prices among producers. Milk is only depooled when the result means more money for the handler who depools. Since by definition Class I milk cannot depool, the Class I sale is always disadvantaged when milk is depooled. In depooling, Class I suppliers are **always** disadvantaged; it is a practice which is beneficial solely to suppliers for Class II, III, and IV. This is the ultimate in irony – that the source of additional value to the pool, Class I milk, is unable to be competitive with other class sales due to depooling. (Gallagher; Exh. 14, pp. 26–30)

27. Proposals 4, 5, and 8 would limit the ability of any producer to repool his milk after depooling for various periods of time. Proposal 4 and 5 would require, in similar ways, that milk from a farm which is depooled may not re-associate with the Order for a 12 month period. Proposal 8 would establish a period of 2 months to 7 months of pool exclusion after depooling.

28. Proposals 6 and 7 address the depooling/repooling problem on a handler basis, rather than a producer basis, by sharply limiting the handler's ability to repool milk, after it has been depooled, to 115% of the prior month's pooling volume in any month (excepting March when the limitation should be 120% to take into account seasonal production increases and the number of days in the months of February and March).

29. The magnitude of the difference in returns from depooling is large. Exhibit 18

Table 2-E shows that in April 2004 a handler which was unable to depool was $3.78 per hundredweight behind in ability to pay versus a handler which was able to depool. (Tr. 245) For the supplier who delivered a tanker load of milk per day to a fluid bottler, that difference amounted to $54,432 for the month; for 10 loads per day $544,320 per month. Differences of this magnitude would be insurmountable for nearly any milk procurer. (Tr. 245)

30. While underwriting risk management tools is not a purpose of federal orders, depooling undermines the ability of dairy farmers to effectively use risk management tools normally available to lock in a blend price. Depooling-caused swings in the PPD are so great that farmers cannot find a willing participant to help them hedge their blend price. This experience was confirmed by the testimony of dairy farmers. (Tr. 370–71)

31. Depooling in 2004 caused reductions in the Order 33 PPD of up to $1.66 per hundredweight. (Exh. 7, Request 5; Tr. 247–48)

32. Proposals 6 and 7 would not eliminate the ability to depool. (Tr. 250–51) They would however place a substantial price on a handler's depooling decision. By exacting a price for the depooling decision, the 115% repooling limit would curb the practice to a meaningful degree. (Tr. 250–51)

The proposal for transportation credits for the Class I market (Proposal 9)

33. Proposal 9 is a proposal for transportation credits. Proposal 9, as modified, would provide credits using the rate of payment of $.0031 per hundredweight per mile ($.0024 in Michigan) on allocated Class I volumes delivered to distributing plants. (Tr. 273–75) This is a rate which is both responsible and reasonable and pushes the market towards efficiency. The proposal would be limited to payment for deliveries of 350 miles; and it would net the pounds paid to any distributing plant against any diversion or transfers made on the same day as a

protection from abuse of the credit. (Tr. 278) Additionally the proposal directs the Market Administrator to make the measure of miles be the shortest distance possible by computing the shortest road miles from the distributing plant to the county seat of the nearest farm on the route. (Tr. 285–86) The handler requesting the credit must provide data to the Market Administrator justifying all calculations. (Tr. 278) Proposal 9 would exempt the first 75 miles from payment, a distance which reasonably represents the current distance which producers delivering to local manufacturing plants pay for hauling. (Tr. 276) This distance would be subject to adjustment by the Market Administrator, after appropriate proceedings, to recognize changes in marketing conditions in the future. (Tr. 279)

34. The proposed mileage limits on the transportation credit are based upon data for the actual costs and distances for hauling in Order 33 and its milkshed. They are calculated to compensate for the Class I supplies while avoiding the potential for abuse.

35. Transportation credits for Class I milk deliveries are needed to restore equity between the suppliers of milk for Class I and all other producers. (Tr. 263) It is a disorderly marketing condition when those producers who supply the Class I milk which creates the blend price are at a competitive disadvantage because they are required to absorb hauling expenses which are not reimbursed by the order.

The need for expedited action.

36. There is a need for this hearing to proceed on an emergency basis. (Tr. 207, 294–95) The issues with depooling will continue to be a problem in the market until they are addressed. (Tr. 294) Opponents who have argued that there is no need for emergency treatment because the concerns are past are engaging in wishful thinking, or worse. Amendments are needed as soon as possible. The concerns with performance standards also have a very short-

term horizon for need. California milk moved very easily through the Order system shifting from one market to the next as regulation changed. The producers in Order 33 have no desire to experience the blend damage that producers in, for instance, Order 30 have from distant western milk and emergency action will help alleviate any possible concern. (Tr. 295)

III. THE POOLING PROVISIONS OF ORDER 33 SHOULD BE AMENDED AS PROVIDED IN PROPOSALS 1 AND 2.

A. The need for enhanced performance requirements in Order 33.

Proposal 1 to prohibit dual pooling should be adopted. There was no objection to the proposal which would simply bring Order 33 in line with other orders, including Orders 30, 1, 32, 124, and 131 which now prohibit pooling of milk which is also pooled on a statewide order with marketwide pooling. But other changes in the performance requirements of Order 33 are called for as well.

The evidence is abundant in this record that the performance requirements in Order 33 require further, additional adjustments. The evidence is in the form of: (1) distant milk supplies which depress the market blend price and do not service the market equitably; (2) performance standards which do not meet the most fundamental tests of economic reality; and (3) continued difficulties in attracting milk to distributing plants in the market. (Tr. 213–214)

The hearing record clearly shows (Exh. 15, Table 3; Exh. 15, Chart 1) that poolings on the Order continue to be well in excess of any reasonable, necessary reserve. These supplies readily flee the market when price relationships make that more economical, and when on the Order they depress the Order's blend price. (Tr. 219; Exh. 7, Request 5)

The Order provisions allow the too-free pooling of milk supplies which do not regularly supply the market.

The recent history of federal order pooling – with California milk dual-pooling on federal orders and with the current pooling of large volumes of Idaho milk in Order 30 – demonstrates that if pooling provisions allow uneconomic attachment of milk supplies, the milk will find its way into the pool. Order 33 must be amended to preclude this possibility and to enhance the competitiveness of producers regularly pooled and supplying the Class I market.

B. Terms of Proposal 2.

There are three enhancements to Order 33 performance requirements in Proposal 2: (1) an increase in the Section 7(c) supply plant shipping percentages; (2) an increase in the Section 7(d) and 7(e) supply plant shipping percentages; and (3) a decrease in the allowable diversions of producer milk to nonpool plants We will review these proposed changes to Order language in turn:

1. Increase in supply plant shipping requirements. Proposal 2 will amend § 1033.7(c) as follows:

> (c) A supply plant from which the quantity of bulk fluid milk products shipped to, received at, and physically unloaded into plants described in paragraph (a) or (b) of this section as a percent of the Grade A milk received at the plant from dairy farmers (except dairy farmers described in § 1033.12(b)) and handlers described in § 1000.9(c), as reported in §1033.30(a), is not less than 40 percent of the milk received from dairy farmers, including milk diverted pursuant to § 1033.13, subject to the following conditions:

The result of this language change is to increase the delivery standard for supply plants by 10% for all months. In light of the data showing that market reserves are still excessive, and blend prices too low to attract a reserve supply or retain a supply from other markets, this modest change in shipping requirements is warranted. These proposed changes will allow the Secretary to increase order requirements beyond those established in the 2001 hearing. Now is the time for this change. No proposals have been offered to reduce performance requirements. Proposal 2 is

a small change in the right direction.

2. Cooperative supply plants and contracted plants. Proposal 2 would amend the performance requirements for Section 7 (d) cooperative supply plants and Section 7 (e) plants as follows:

> (d) A plant operated by a cooperative association if, during the months of August through November, 40 percent and during the months of December through July, 30 percent or more of the producer milk of members of the association is delivered to a distributing pool plant(s) or to a nonpool plant(s), and classification other than Class I is not requested. Deliveries for qualification purposes may be made directly from the farm or by transfer from such association's plant, subject to the following conditions:
>
> (1) * * *
>
> (2) The 30 percent delivery requirement for December through July may be met for the current month or it may be met on the basis of deliveries during the preceding twelve (12) month period ending with the current month.
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> * * *
>
> (e) * * *
>
> (1) The aggregate monthly quantity supplied by all parties to such an agreement as a percentage of the producer milk receipts included in the unit during the months of August through November is not less than 45 percent and during the months of December through July is not less than 35 percent;

This proposal results in an increase in required deliveries from Section 7 (d) and (e) plants of 10% during the peak shipping months of August through November; and for the cooperative 7(d) plants establishes a "hard" performance minimum during those months which is not subject to the allowance for a 12 month rolling average.

3. Diversion limitations. Proposal 2 limits diversions of producer milk as follows:

> (d) * * *

> (4) Of the total quantity of producer milk received during the month (including diversions but excluding the quantity of producer milk received from a handler described in § 1000.9(c) or which is diverted to another pool plant), the handler diverted to nonpool plants not more than 50 percent in each of the months of August through February and 60 percent in each of the months of March through July.

This language decreases the allowable percentage of diversions of producer milk by 10% during all months of the year.

C. The standards for appropriate performance requirements.

The appropriate standards for federal order pooling and performance requirements have been articulated and refined by the Secretary in a number of post-federal order reform decisions. For instance, in a 2001 decision, the Secretary stated at 68 Fed. Reg. 51644–45, August 27, 2003:

> The pooling standards of all milk marketing orders, including the Central order, are intended to ensure that an adequate supply of milk is supplied to meet the Class I needs of the market and to provide the criteria for identifying those who are reasonably associated with the market as a condition for receiving the order's blend price. The pooling standards of the Central order are represented in the Pool Plant, Producer, and the Producer milk provisions of the order. Taken as a whole, these provisions are intended to ensure that an adequate supply of milk is supplied to meet the Class I needs of the market. In addition, it provides the criteria for identifying those whose milk is reasonably associated with the market by meeting the Class I needs and thereby sharing in the marketwide distribution of proceeds arising primarily from Class I sales. Pooling standards of the Central order are based on performance, specifying standards that, if met, qualify a producer, the milk of a producer, or a plant to share in the benefits arising from the classified pricing of milk.
>
> Pooling standards that are performance-based provide the only viable method for determining those eligible to share in the marketwide pool. That is because it is the additional revenue from the Class I use of milk that adds additional income and it is reasonable to expect that only those producers who consistently bear the cost of supplying the market's fluid needs

> should be the ones to share in the distribution of pool proceeds.
> …
>
> Pooling standards are needed to identify the milk of those producers who are providing service in meeting the Class I needs of the market. If a pooling provision does not reasonably accomplish this end, the proceeds that accrue to the marketwide pool from fluid milk sales are not properly shared with the appropriate producers. The result is the unwarranted lowering of returns of those producers who actually incur the costs of servicing and supplying the fluid needs of the market.

These principles have been recently reiterated in the Tentative Final Decision issued for Order 30 with respect to certain pooling and performance issues in that order. The Secretary stated:

> The pooling standards of all Federal milk marketing orders, . . . are intended to ensure that an adequate supply of milk is available to meet the Class I needs of the market and to provide the criteria for identifying the milk of those producers who are reasonably associated with the market as a condition for receiving the order's blend price. The pooling standards of the . . . order are represented in the Pool Plant, Producer, and the Producer milk provisions of the order and are performance based. Taken as a whole, these provisions are intended to ensure that an adequate supply of milk is available to meet the Class I needs of the market and provide the criteria for determining the producer milk that has demonstrated service to the Class I market and thereby should share in the marketwide distribution of pool proceeds.
>
> Pooling standards that are performance based provide the only viable method for determining those eligible to share in the marketwide pool. It is primarily the additional revenue generated from the higher-valued Class I use of milk that adds additional income, and it is reasonable to expect that only those producers who consistently bear the costs of supplying the market's fluid needs should be the ones to share in the returns arising from higher-valued Class I sales so that costs can be recovered.
>
> Pooling standards are needed to identify the milk of those producers who are providing service in meeting the Class I needs

> of the market. If a pooling provision does not reasonably accomplish this end, the proceeds that accrue to the marketwide pool from fluid milk sales are not properly shared with the appropriate producers. The result is the unwarranted lowering of returns to those producers who actually incur the costs of servicing and supplying the fluid needs of the market.
> 70 Fed. Reg. at 19715 (April 14, 2005)

These cooperatives respectfully suggest that these same principles and standards should be applied in this proceeding to adopt the order amendments put forward in Proposal 2.

D. The White Eagle et al objections and the Cotterill market structure assertions.

The White Eagle Federation opposed the adoption of Proposal 2, or any tightening of Order 33 pooling standards. We must observe, at the outset, that while certain management and consultant representatives of these producer groups testified, there were no dairy farmer members heard from. This may well have been because the positions articulated by management are not well understood by and not representative of grass roots farmer sentiment. For instance, it is rather clear that pooling of milk from outside the Order 33 area is not a popular practice with dairy farmers in Order 33. It is doubtful, therefore, that any indigenous Order 33 members of White Eagle cooperatives knowingly support, for example, the continued pooling of milk of Alto Dairy or Family Dairies USA from Wisconsin, Iowa, and/or Minnesota on Order 33.

Furthermore, the White Eagle testimony made clear that it is pooling essentially to the limit of the current performance requirements; thus confirming that its primary market is for sales to non-Class I uses. It is clear that White Eagle's opposition to Proposal 2 seeks to preserve the status of its manufacturing use sales — as pooled sales sharing in the Class I proceeds. The testimony of Mr. Leeman for White Eagle reveals that its commitment of cooperative member milk to the Class I market is at best about 30%[1], a performance level which

[1] This utilization follows from Mr. Leeman's testimony that: (1) White Eagle pools a monthly total of about 150 million pounds; (2) 20% (30 million pounds) of this volume is

is surely “inadequate”, under the Department’s articulated standards, in a market which requires the importation of milk both internally (from surplus to deficit areas within the Order) and externally (by seasonal shipments from out of the order). Proposal 2's enhancement of the current “inadequate” standards for pooling on Order 33 would only require a wholly reasonable increase of about 10% in performance by White Eagle Cooperative members.

The primary opposition testimony for White Eagle et al was made by Dr. Ronald Cotterill of the University of Connecticut. Dr. Cotterill testified, not as an expert in milk marketing or federal orders[2], which he is not, but as a university economist who has studied dairy product pricing practices, primarily at the supermarket level. The Cotterill objection to Proposal 2 was based upon competitive industrial market structure theory rather than any study of Order 33 (or for that matter any study of the pooling terms and practices in any milk order). He opined that Proposal 2 should not be adopted because it would enhance the market position of non-White Eagle pooling federations, or common marketing agencies, in particular, Dairy Marketing Services (DMS). Apparently, in Dr. Cotterill’s view, this competitive structure objective should supercede any other principle of federal order pooling standards, such as those articulated by the Secretary and quoted above. The view seems to be that “market structure,” rather than performance, should dictate pooling provisions. There are a number of problems with, and deficiencies in, Dr. Cotterill’s analyses in this proceeding.

First, his analysis ignores the AMAA. By focusing on market structure, ostensible

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independent distributing plant milk of Superior Dairy and United Dairy; (3) White Eagle’s aggregate monthly distributing plant deliveries are 60 to 70 million pounds; (4) therefore, of the 120 million pounds of White Eagle cooperative milk, only 30 to 40 million or 25 to 33% is delivered to pool distributing plants.

[2] Dr. Cotterill’s lack of expertise in milk marketing matters sharply contrasts with the recognized expertise of witnesses such as Mr. Gallagher (Tr. 188–89) and Mr. Christ (Tr. 1062–63).

market shares, and principles of industrial organization and competition theory[3], Dr. Cotterill essentially ignores the purposes and standards of the AMAA which displaces the otherwise dysfunctional "free market" in raw milk sales with a system of market order pools. The structure of such pools is necessarily going to be different, and operate differently, from industrial free markets dealing in manufactured or processed goods. Orderly marketing, in a milk order pool, is not a concept that one will find in the literature of industrial competition theory; but it is the single overriding objective of federal milk order pools.

Secondly, and just as significantly, Dr. Cotterill's testimony about present alleged anti-competitive practices, and conclusions about possible adverse effects of Proposal 2, were shown to be little more than ivory tower speculation, not conclusions made on the basis of market knowledge and expertise. For instance, the basis for his assertion that "fluid milk processors currently supplied by the DFA led system may not be receiving the same terms as larger processors" (Exh 31, p. 10; Tr. 782) was that (1) he is aware of unconfirmed reports in New England that such price discrimination occurred; and (2) that such price discrimination "can be profitable." (Tr. 850) In the end, he had absolutely no factual basis for the assertion; solely his intellectual musings. As such his comments may or may not be of some academic interest,

[3] A full critique of the inappropriateness of use of industrial market share assumptions in federal milk order market performance analysis is beyond the scope of this brief, or this hearing. We would point out, however, that attributing market power to nominal "pool" percentages (such as Dr. Cotterill does for DMS, MMPA, et al) completely ignores that "pooling" of milk has no permanency, as does ownership of proprietary technology (Microsoft) or natural resources (OPEC), for instance. Pooling affiliations change from year to year, and even from month to month in milk markets; they are based on contractual relationships which are subject to regular renegotiation. Consequently, to compare DMS's market position to that of Microsoft, as Dr. Cotterill did (Tr. 832), borders on the ridiculous. We would observe, for instance, that Order 33 is so blockaded to competition that White Eagle was just formed a few years ago and has already achieved a 12% pooling market penetration. What new competitor has achieved a 12% share of the PC operating system market?

but surely they do not provide the type of substantial evidence upon which milk order decisions must be based. E.g., Borden Inc. v. Butz, 544 F.2d 312 (7th Cir. 1976)(Rejecting "hortatory, conclusory and speculative opinions and predictions" as a basis for a milk order decision); see also, Fairmont Foods Co. v. Hardin, 442 F.2d 762 (D.C.Cir 1971).

White Eagle and the Jacoby Group wish to have the ability to pool as much milk as they can on Order 33 while selling the majority to manufacturing plants inside and outside the Order. This is not a new or unknown practice in milk marketing; it is indeed a common practice. But the Secretary must set the rules; and here, the rules need to be adjusted, as proposed in Proposal 2, in order that the objectives of the Act for orderly marketing are achieved.

IV. OPEN DEPOOLING IN ORDER 33 SHOULD BE LIMITED THROUGH THE ADOPTION OF PROPOSAL 7.

A. Proposal 7's limitations on repooling of depooled milk should be adopted**.**

1. The depooling/repooling problem. Depooling has become a problem of orderly marketing in federal orders which goes to the heart of the order system. The huge swings in volumes of milk pooled, up to half of the total volume of milk on Order 33 being pooled or depooled from month to month, is such that it almost makes a mockery of the system. Because depooling has economic results which are profitable to the depooler, all entities, including the cooperatives submitting this brief, when possible, have depooled supplies of milk from time to time. All of these organizations recognize, however, that the permissibility of open and free depooling must come to an end in the interest of orderly marketing for the system as a whole.

We want to briefly discuss several of the orderly marketing issues which depooling

creates. The record documenting these problems is virtually uncontroverted and is a clear mandate for the requested adoption of Proposal 7. There are three marketing problems relating to depooling which we would like to highlight:

First, depooling creates a lack of uniform returns among dairy farmers. There is a wide array of testimony in this record with respect to the disorderliness resulting from the lack of uniformity of producer returns created by depooling. The uniformity issues were described both by the cooperative witnesses, and by the individual dairy producers. The differences in pay prices among producers because of depooling can be of the order of several dollars per hundredweight. These are substantial, meaningful and quite disorderly marketing conditions which must be remedied. Persistence, without remedy, of such conditions undermines and corrodes producer support for federal orders.

Secondly, the free and open depooling of milk exacerbates the problem of availability of milk for Class I uses in Order 33. It almost goes without saying that milk which moves on and off of the pool in relationship to changes in the configuration of Class prices is unavailable for the fluid market. Being part of the federal order pool should require a commitment to availability for Class I beyond that which free depooling involves. Particularly in Order 33, where there is a documented problem with the availability of supplies to the distributing plants in the Order, depooling-at-will should not be part of the terms of participation in the pool.

Finally, as several witnesses testified, depooling's contribution to huge swings in the PPD creates marketing problems for producers who are dedicated to supplying the Order and wish to avail themselves of risk management strategies. It is important to understand the dynamics here: hedging milk prices with dairy futures or options contracts is <u>not</u> a strategy which can avoid or ameliorate the impact of depooling. To the contrary, the impact of depooling

on the PPD interferes with the ability of dairy farmers to hedge the inherent price fluctuations in the dairy product markets. In other words, depooling exacerbates – to a degree that is beyond any risk management strategy's control – the variations in milk prices.

In summary, to further price uniformity among producers, to make milk supplies that are pooled in the Order more regularly available for Class I utilization, and to allow producers the ability to manage the inherent risk in dairy product markets more readily, there must be amendments to Order 33 to limit depooling of milk.

2. The Proposal 7 Solution. The Proposal 7 limitation on depooling represents a substantial change in order regulations which has been criticized by other participants as being insufficient change, on the one hand, or providing for too much change, on the other. We believe that the degree of limitation of repooling which Proposal 7 provides is appropriate for this market at this time.

Proposal 7 does not eliminate depooling. It simply limits the ability of a handler to immediately repool the depooled milk by placing a 115% (120% in March[4]) limitation on increases in pooling from month to month. A handler can, when depooling is lucrative, eliminate whatever portion of his milk he chooses from the pool and pocket the short term revenue enhancement. However, the handler will need to be aware that he will need to phase his dedicated manufacturing milk back into the pool over a period of time after it has been depooled. Exhibit 7, Request 12, shows that the handler could depool up to 34 % of his manufacturing milk and have 100% re-pooled within three months after the initial depooling. However, to the extent

[4] The 120% figure for March is a modification of the proposal as noticed in the hearing. It is appropriate on the basis of the record evidence with respect to seasonal changes in daily production from February to March and the variation in the number of days in the month. Proposal 7 is not intended to create pooling problems for regular suppliers of the market.

that more than 34 % was depooled, the handler would need more than three months to get all milk back on the pool (unless, of course, it is delivered to Class I distributing plants where it would automatically be pooled).

These cooperatives have evaluated all of the potential options that were in the hearing notice (and others that were not) for addressing the disorder of open depooling. They considered proposals for other market provisions similar to Proposals 4, 5, and 8. They considered greater percentages for the repooling limitation such as 125% as proposed for Orders 30 and 32. After analyzing these options and taking into account the operations of servicing the Order 33 market regularly, it is submitted that Proposal 7 best fits the market. The proposed language on depooling is:

Amend § 1033.13 by adding new paragraphs (e)(1) through (e)(4) to read as follows:

§ 1033.13 Producer milk.

* * * * *

(e) The quantity of milk reported by a handler pursuant to § 1033.30(a)(1) and/or § 1033.30(c)(1) for the current month may not exceed 115 percent of the producer milk receipts pooled by the handler during the prior month (120% during the month of March). Milk diverted to nonpool plants reported in excess of this limit shall be removed from the pool. Milk received at pool plants in excess of the 115 percent limit, other than at pool distributing plants, shall be classified pursuant to § 1000.44(a)(3)(v). The handler must designate, by producer pick-up, which milk is to be removed from the pool. If the handler fails to provide this information the provisions of 1033.13(d)(6) shall apply. The following provisions apply:

(1) Milk shipped to and physically received at pool distributing plants shall not be subject to the 115 percent limitation;

(2) Producer milk qualified pursuant to § ____.13 of any other Federal Order in the previous month shall not be included in the computation of the 115 percent limitation; provided that the producers comprising the milk supply have been continuously pooled on any Federal Order for the entirety

of the most recent three consecutive months.

(3) The market administrator may waive the 115 percent limitation:

(I) For a new handler on the order, subject to the provisions of § 1033.13(e)(4), or
(ii) For an existing handler with significantly changed milk supply conditions due to unusual circumstances;

(4) A bloc of milk may be considered ineligible for pooling if the market administrator determines that handlers altered the reporting of such milk for the purpose of evading the provisions of this paragraph.

Proposal 7 represents an effective, but moderate, current solution for the depooling problem. It has important safeguards to allow milk to be delivered to distributing plants and to allow new handlers to come into the Order. Proposal 2 is a step forward for orderly marketing which the Department should take.

B. Objections and Objectors to Proposal 7**.**

1. The general objections to any limit on depooling. There was precious little testimony at this hearing in opposition to limits on depooling. However, the general objections need to be commented upon briefly. Some objections have been inferred to any limitation on depooling on the grounds that pooling means a one-way flow of revenue from Class I handlers to other users. We do not believe that this is a principle of federal orders, or that it should be. If the only purpose of federal order marketwide pools was to blend Class I revenues, one would assume that there would be no pricing or pooling of any other uses; but that is not the case. All use values are blended to derive a uniform minimum producer price, blend price or PPD. The AMAA does not authorize only classifying, pricing and pooling Class I uses; it authorizes pooling of ***all*** uses of milk. 7 U.S.C. § 608c(5)(B)(ii), the statutory authority for marketwide pools, directs "the

payment to all producers and associations of producers delivering milk to all handlers of uniform prices for all milk so delivered, irrespective of the uses made of such milk by the individual handler to whom it is delivered . . . " There is simply no basis in this argument.

Any arguments that open depooling and repooling have always been the practice in federal orders, are not correct and, in any event, should not impede the correction of an order malfunction. In fact, the inequity of depooling and repooling has been addressed in other orders (e.g. Order 1's post-reform dairy farmer for other markets provision) and in the federal order reform decision (price announcements were advanced to limit price inversions which contribute to depooling). The fact that the problem has not been cured should certainly not prevent its being addressed here.

2. National All Jersey and the White Eagle Federation. These organizations apparently have the same or similar motivations as others. To the extent that they actually market milk, they do so primarily for manufacturing uses, Class III or IV, but want to take advantage of the Class I market when it is lucrative, while having nothing to do with it when it is not to their economic advantage. In our view, there is neither equity in this position nor statutory authority for it.

The contentions that depooling and negative PPDs are national issues which should not be addressed in Order 33 or any one order should not be adopted. First of all, the Secretary has made it abundantly clear that pooling provisions of each order are the products of marketing conditions in those orders. Each order has different marketing conditions and therefore requires different pooling provisions. Even though certain pricing policies in the federal order, such as advanced pricing of Class I milk, contribute to price inversions and these pricing programs are national, nevertheless, the pooling and depooling provisions in each order need to accommodate

market conditions in that order in their own unique way. There is no reason, in fact it would be wholly unjustified, to await an as yet unrequested and likely never-to-be-conducted national hearing to synchronize pricing of all classes before addressing the present extremely disorderly conditions in Order 33 created by open depooling provisions in the Order.[5]

The disorderliness of open depooling needs to be fixed and needs to be fixed now before the next price inversion occurs and its accompanying disorder discredits the Order program further.

3. The Dairy Farmer for Other Markets (DFOM) Proposals. In our view, the DFOM proposals go too far, too fast for Order 33 in 2005 in addressing the problem of depooling. Depooling is an industry practice which has evolved over a number of years. It has transformed from a practice limited in geographic scope to the outlying areas of upper midwestern orders in the 1970s to its current must-do competitive status, a near-national feeding frenzy in times of price inversions. In this context, Proposal 7 has been crafted as a very substantial change in permissible practices; but not a night-to-day change of the magnitude which would be represented by adoption of Proposals 4 or 5 in Order 33.

All DFOM proposals have the "scarlet letter" problem of limiting pooling to producers who are eligible on the basis of pooling decisions made by handlers. We believe that they could be subject to abuse by handlers who would have the ability to depool a producer, thereby locking him out of the market for a year, who, for instance, has stated his intention to switch marketing organizations or affiliations. This could be addressed by revising the proposals to only apply to the same handler's pooling of the producer or producers. But, in that circumstance, it would

[5] The Secretary should not give any credence to the arguments of any parties who request the indefinite preservation of inequitable pooling rules because there is a theoretical fix which they did not request for this hearing.

lend itself to the possibility of handlers swapping groups of producers for pooling purposes. Proposal 7 has language which would allow the Market Administrator to address such abuses; Proposals 6 and 8 do not.

We recognize that there is both a certain simplicity and strictness in the operation of DFOM proposals which lends credence to their appeal. However, all things considered, we remain of the view that Proposal 7 provides the best mechanism for addressing open depooling in Order 33 at this time.

V. PROPOSAL 9 FOR TRANSPORTATION CREDITS ON DIRECT-SHIPPED CLASS I MILK SHOULD BE ADOPTED.

A. The problem of servicing Class I in Order 33.

The orderly functioning of Order 33 requires the adoption of transportation credits for Class I milk as requested in Proposal 9. There are two principal reasons for this. First, as the record shows, supplemental milk supplies from within and without the order are required for servicing the Order's Class I needs. Because there is a great disparity among the Class I suppliers in shouldering the transportation costs required for delivery to the markets, there is currently a embedded difference in returns for Class I usage in the market among Class I suppliers. In addition, this market, like others such as Order 30 with heavy manufacturing sectors, inherently, although not by design, disfavors the Class I suppliers, without the benefit of transportation credits to offset a portion of the greater cost of transporting milk to Class I markets. We will discuss each of these points in turn.

First, the detailed information about the DFA experience in Fall 2004 milk supply costs is illustrative of the supplemental needs and costs. In October, DFA purchased 21,612,207 pounds of supplemental milk from four out-of-area states for delivery to Class I customers in

Order 33. (Others may have also made some purchases of supplemental milk for their customers, but the information details DFA's experience solely.) Supply arrangements were coordinated through the Mideast Milk Marketing Agency, MEMA, for efficiency of transport and purchase. While supplemental supplies are very expensive with respect to over order charges[6], Proposal 9 does not contemplate any reimbursement for costs other than a portion of the transportation cost, which is not currently being covered by the Order. The October DFA milk was sourced from nine different suppliers in Michigan, Illinois, Minnesota and Wisconsin. The loads were delivered to a number of different customers in Indiana, Ohio and Pennsylvania. The table identifies the following details: 1.6 million pounds of milk was purchased from Illinois suppliers and delivered to Ohio customers. On average, this milk supply was transported 593 miles and had a cost of $2.02 per loaded mile. 0.7 million pounds of milk was purchased from Michigan suppliers and delivered to Ohio and Pennsylvania customers. On average, this milk supply was transported 278 miles and had a cost of $2.35 per loaded mile. 19.3 million pounds of milk was purchased from Minnesota and Wisconsin suppliers and delivered to Indiana, Ohio and Pennsylvania customers. On average, this milk supply was transported 368 miles and had a cost of $2.55 per loaded mile. For the entire milkshed, the range of average rates per loaded mile was $2.37 for Ohio deliveries, $2.54 for Indiana deliveries and $2.55 for Pennsylvania deliveries. The market average of $2.51 is heavily influenced by the deliveries from Minnesota and Wisconsin. Mr. Gallagher testified that these charges, while taken from October business records, are typical for the entire fall short supply season. These supplemental milk expenses are

[6]Exh. 15, Table 6, depicts transport cost alone. Every purchased load had additional costs associated with it. For all of these loads there was a give up or premium paid over the full Federal Order value. Some of the loads purchased were made on a multi-month contractual basis and some were spot market purchases. The fees above transport costs ranged from slightly below $1.50 per hundredweight to over $3 per hundredweight.

borne only by the supplier and any voluntary members of the MEMA superpooling agency. But the Class I sales values are shared marketwide.

Within Order 33 milk must move from reserve supplies in Michigan and Northern Ohio to the remainder of the market. The ratio of production to Class I use in the Michigan region shows that 64 percent of the supply is available for reserve supply for other regions, 464.6 million pounds of producer receipts minus 166.8 million pounds of Class I sales with the result divided by 464.6 million pounds of producer receipts. The same calculation for the Northern Ohio region produces a reserve supply ratio of 69 percent. For the Pennsylvania region, the calculation is only 24 percent, barely enough reserve to service some of this region's needs. The Indiana region's ratio is 17 percent, again minimal. Due to the north/south divide in Indiana relative to production and sales, milk must be imported, and has been since the 1980's, from outside of Indiana to supply the sales in the southern half of the state. The Southern Ohio region is deficit 73.1 million pounds of milk to meet sales needed for October. MA Exhibit 7, DFA Request 8(a) through (e). Supplemental milk movements from the in-area surplus regions to the regions requiring imports travel significant miles. Typical distances for movements from in-area reserve supplies in Central Michigan would be 317 miles to Newark, Ohio, Kroger; 349 miles to Sharpsville, Pennsylvania, Dean; 365 miles to Newport, Kentucky; Trauth, and 303 miles to Akron, Ohio; Dean. For movements out of the reserve supply areas in Northern Ohio, distances would range from 86 miles in Newark, Ohio; 133 miles to Sharpsville, Pennsylvania, and 200 miles to Newport, Kentucky.

The current Order's differentials do not pay for these milk movements. The zone layout in Order 33 is wide and flat and is reflective of the Cornell model used by USDA in establishing the Class I differential grid used under Federal Orders. Because of its current flat nature, the

Order 33 zone structure does not offer enough incentive to attract or move milk to Class I locations within the market. While milk does cross zones to deliver to pool distributing plants, the additional $0.20 spread between each zone does not offer enough incentive to pay for the delivery. This can be seen in MA Exhibit 7, DFA Request Numbers 16 and 17. Only 20 percent of the milk produced in the $1.80 zone moves to plants in the $2.00, $2.10, $2.20 or $2.30 zones. A reason for this is the cost of moving the milk is far greater than the Order's zone adjustment. For example, the average hauling distance for $1.80 zone produced milk delivered to the $2.20 zone is 215 miles. For a load with 48,000 pounds of milk and a cost of $2.20 per loaded mile, the additional cost of moving the milk is $0.66 per hundredweight, calculated by 215 miles minus 71 miles (the 71 miles is the average hauling distance for deliveries in the $1.80 zone) times $2.20 per loaded mile divided by 480 hundredweight. This compares to the Order's zone incentive of moving the milk of $0.40. Since much of the in-area reserve is located in Michigan and Northern Ohio, there is an increasing need to transport milk from northern areas of the Order to the southern areas. Transportation credits tailored to transactional events will help offset the cost associated with these movements. This failure of the Order to have a mechanism to assist Class I suppliers in covering these costs related to Class I markets places Class I suppliers at a competitive disadvantage in the field with pay prices relative to those milk supplies not heavily serving the Class I market. Yet all producers benefit equally via the pooled returns Class I generates.

Taken in aggregate, these data establish that the average cost to deliver milk to Class I plants within the order on a day to day basis is less than the average cost to deliver milk to manufacturing outlets. This situation, depicted generally on Exh. 7. Request 7, compiled by the Market Administrator, was discussed in testimony by, among others, Mr. Christ. (Tr. 1084–93).

The result is an embedded disadvantage for Class I suppliers as a group. Surely, in a marketwide pool, it is a disorderly marketing condition to have Class I suppliers placed at an inherent disadvantage by virtue of the transportation expenses which they must incur and which benefit the entire market. Transportation credits as in Proposal 9 can even out this disparity, at least in part, and restore a more orderly contour to the marketplace.

Mr. Gallagher explained, and documented, how these proponents are not able to overcome this market dysfunction through over order pricing and pooling programs. The Mideast Milk Marketing Agency (MEMA) operates an over order pricing and supplemental supply program for Class I sales in a major portion of Order 33[7]. The participating MEMA cooperatives charge Class I customers as high an over order Class I price as can be negotiated. With this price the suppliers are responsible for providing the market's needs for Class I uses when needed, as needed. The cost of acquiring supplemental seasonal and weekly fluctuating amounts is substantially due in no small part to the lack of availability of local Order 33 area milk which is dedicated to non-fluid uses. When the cost of acquiring, transporting, and delivering the supplemental supplies is netted from the over order charges collected, DFA, the largest MEMA member has net proceeds available to pay its dairy farmers which are significantly less than the prevailing premiums paid to local Order 33 producers, such as Mr. Baer, or the suppliers to Smith Dairy, who are not members of DFA or other MEMA cooperatives. (Gallagher Tr. 1121–29; Baer Tr. 1051–59; Soehnlen Tr. 1097--98)

Proposal 9 would redress only a portion of the current market disorder which places the Class I suppliers in Order 33 at a competitive disadvantage in the marketplace.

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[7] A similar program is operated in Michigan as the Producer Equalization Committee (PEC).

B. The proposed transportation credit language.

The Order language for Class I transportation credit which we propose is as follows:

Insert a new Section 1033.55:

1033.55 Transportation Credits.

(a) each handler operating a pool distributing plant described in Section 1033.7(a) or (b) that receives milk from dairy farmers, and each handler described in Section 1033.9(c) that delivers milk to a pool distributing plant described in Section 1033.7(a) or (b) shall receive a transportation credit on the portion of such milk eligible for the credit pursuant to paragraph (b) of this section.

(1) transportation credits paid pursuant to paragraph (a)(1) or (2) of this section shall be subject to final verification by the Market Administrator pursuant to Section 1000.77.

(2) in the event that a qualified cooperative association is the responsible party for whose account such milk is received and written documentation of this fact is provided to the Market Administrator pursuant to Section 1033.30(c)(3) prior to the date payment is due, the transportation credits for such milk computed pursuant to this section shall be made to such cooperative association rather than to the operator of the pool plant at which the milk was received.

(b) Transportation credits shall apply to the pounds of bulk milk received directly from the farms of producers at pool distributing plants determined as follows:

(1) determine the total pounds of producer milk physically received at the pool distributing plant.

(2) Subtract from the pounds of milk described in paragraphs (b)(1) of this section the pounds of bulk milk transferred or diverted from the pool plant receiving the milk if milk was transferred or diverted to a nonpool plant on the same calendar day that the milk was received. For this purpose, the transferred or diverted milk shall be subtracted from the most distant load of milk received, and then in sequence with the next most distant load until all of the transfers have been offset; and

(3) multiply the pounds determined in (b)(2) by the Class I utilization of all producer milk at the pool plant operator as

described in Section 1000.44. The resulting pounds are the pounds upon which transportation credits, as determined in paragraph (c) of this section, shall be applicable.

(c) transportation credits credits shall be computed as follows:

(1) determine an origination point for each load of milk by locating the county seat of the closest producer's farm from which milk was picked up for delivery to the receiving pool plant.

(2) determine the shortest hard surface highway distance between the receiving pool plant and the origination point.

(3) subtract 75 miles from the lesser of the mileage so determined in paragraph (c)(2) or 350 miles.

(5) Multiply the remaining miles so computed by 0.31 cents or $0.0031 dollars; provided that for deliveries from farms in the state of Michigan to plants in Michigan, the rate shall be 0.24 cents or $.0024 dollars.

(6) Subtract the Class I differential specified in Section 1000.52 applicable for the county in which the origination point is located from the Class I differential applicable at the receiving pool plant's location.

(7) subtract any positive difference computed in paragraph (c)(6) of this section from the amount computed in paragraph (c)(5) of this section, and

(8) multiply any positive remainder computed in paragraph (c)(7) by the hundredweight of milk described in paragraph (b)(3) of this section.

(d) the rate and mileage limits of paragraphs (c)(3) and (5) of this section may be increased or decreased by the Market Administrator if the Market Administrator finds that such adjustment is necessary to better reflect actual conditions present in the marketplace. Before making such a finding, the Market Administrator shall investigate the need for adjustment either on the Market
Administrator's own initiative or at the request of interested parties. If the investigation shows that an adjustment might be appropriate, the Market Administrator shall issue a notice stating that an adjustment is being considered and invite data, views and arguments. Any decision to revise either figure must be

issued in writing at least one day before the effective date.

(e) for purposes of this section, the distances to be computed shall be determined by the Market Administrator using the shortest available state and/or Federal highway mileage. Mileage determinations are subjected to redetermination at all times. In the event a handler requests a redetermination of the mileage pertaining to any plant, the Market Administrator shall notify the handler of such redetermination within 30 days after the receipt of such request. Any financial obligation resulting from a change in mileage shall not be retroactive for any periods prior to the redetermination by the Market Administrator.

(2) amend Section 1033.60 by amending the introductory paragraph and adding a new paragraph (k) to read as follows:

1033.60 Handler's Value of Milk. For the purpose of computing a handler's obligation for producer milk, the Market Administrator shall determine for each month the value of milk of each handler with respect to each of the handler's pool plants and of each handler described in Section 1000.9(c) with respect to milk that was not received at a pool plant by adding the amounts computed in paragraphs (a) through (I) of this section and subtracting from that total amount the value computed in paragraphs (j) and (k) of this section. Unless otherwise specified, the skim milk, butterfat and the combined pounds of skim milk and butterfat referred to in this section shall result from the steps set forth in Section 1000.44(a), (b) and (c) respectively, and the nonfat components of producer milk in each class shall be based upon the proportion of such components in producer skim milk. Receipts of non-fluid milk products that are distributed as labeled reconstituted milk for which payments are made to the producer-settlement fund of another Federal Order under Section 1000.76(a)(4) or (d) shall be excluded from pricing under this section.
. . .

(k) compute the amount of credits applicable pursuant to Section 1033.55.

We wish to make a number of comments about the specifics of the order language:

1. Handler responsibility. It is intended that each handler would compute and apply for credit as appropriate at pool time. Each handler would have to maintain a file of locations and distances and perform the various computations. While somewhat cumbersome to initially

establish, the task can easily be accomplished with computer aid. The Market Administrator would accept and make payments and then audit as necessary.

2. Limits on reimbursement. The proposed reimbursement rate is tailored to current marketing conditions in Order 33 and designed to be conservative in structure for starters in this order. We recognize that higher rates of reimbursement have been allowed in other proceedings, such as in the recent Hurricane cost recovery in the Southeast, and have not requested those levels of reimbursement here at this time. Likewise, with respect to mileage, it is tailored to the conditions in Order 33 where we believe it is equitable and reasonable to exempt from the credit the mileage that producers pay for delivery to plants in the heaviest production sectors of the milkshed. In this proposal, that mileage is 75 miles. Furthermore, the limit on miles reimbursed should be 350. This should eliminate any abuse possible in making longer than necessary distant shipments and claiming pool reimbursement. The Market Administrator discretion provision provides the mechanism for future adjustment in these compensation factors.

3. Michigan modification. The state of Michigan allows transport of larger loads of milk, farm to plant, than do other states in Order 33. This allows for lower costs of moving milk within the state. Therefore, the rate of reimbursement for Class I milk movements in the state of Michigan should be adjusted accordingly and the proposed language in Section 1033.55(c)(5) would accomplish that. (Rasch Tr. 572–575)

4. Market Administrator discretion. Proposal 9 provides authority for the Market Administrator to adjust, after providing notice to, and receiving comment from, the industry, certain of the marketing-condition specific provisions of transportation credits, including the rate and mileage limitations. This is important language which would embed the Order with an efficient mechanism for updating the details of the transportation credit system.

5. Applicability to direct ship milk only. Proposal 9 provides credits for direct farm shipped milk only. It would not provide credits for supply plant milk shipments. Foremost Farms proposed a modification to Proposal 9 which would extend it to supply plant shipments for Class I uses[8]. Michigan Milk opposed this provision and articulated the basic reason why the proposal as written did not include supply plant milk: That payments from the pool should only be made for the most efficient form of delivery which is farm-direct. (Rasch Tr. 1105–1107)

VI. THE PROPOSALS SHOULD BE ADOPTED ON AN EMERGENCY BASIS.

While no one can predict with certainty the future direction and rate of movement of milk prices, there is nothing in the hearing record to suggest that volatility is going to decline and events since the hearing have already confirmed this fact. Consequently, the circumstances which lead to depooling will remain, and all of the disorder which depooling has meant will continue until amendments have been adopted. At the same time, the potential double whammy of distant milk depressing the Order's blend will remain a present danger. Furthermore, the lack of sufficient incentives in the Order to attract milk to Class I and compensate suppliers for those deliveries will continue to impair the functioning of the Order. Proposals 1, 2, 8, and 9 (as modified herein) should be implemented on an emergency basis, without requiring a recommended decision.

VII. BRIEF IN SUPPORT OF OBJECTIONS AT THE HEARING

These cooperatives, granted an automatic exception to objections made, but overruled, at the hearing, hereby request that the Secretary reconsider the action upon such objections in

[8] DFA takes no position on the Foremost modification.

accordance with the Rules of Practice. See 7 C.F.R. §§ 900.8(d) and 900.9(b).

The testimony, written by counsel (Tr. 715–16), but read by the witness for White Eagle, should be stricken from the record; and the exhibits offered with the statement excluded. (Tr. 688–89) Testimony at these hearings must be upon oath or affirmation (7 C.F.R. § 900.8(d)(I)); and "shall" be excluded if "not of the sort upon which responsible persons are accustomed to rely." 7 C.F.R. § 900.8(d)(iii). Mr. Leeman did not prepare any of his direct testimony. (Tr. 714–16) He could not explain numbers asserted within the statement. (Tr. 711–716) He did not prepare the exhibits; did not know that they were not complete downloads of industry websites; and did not know that, while represented as downloads, the exhibits had editorial insertions, apparently inserted by the downloader, but not identified as additions or embellishments. (Tr. 937–938) Furthermore, Mr. Leeman refused to identify the entities on whose behalf he was purporting to speak. (Tr. 694–95) This material, and the accompanying testimony, cannot possibly be described as information "of the sort upon which responsible persons are accustomed to rely" and it should be excluded by the Secretary from the record upon which the Decision in these proceedings will be based.

Furthermore, we reiterate our more general objection to the admission into these proceedings of selected printouts of industry websites. (Tr. 689) The use which is being made in these proceedings of selected web pages of industry participants does not add probative information[9] to the record and burdens participants with the need to review and respond to materials taken out of context, or worse, edited in some cut-and-paste fashion, as proposed Exh.

[9] The purpose is most frequently ***ad hominem*** attacks on the "party", its structure and general business affairs, as opposed to information about conditions in the marketing area at issue.

30. The evidentiary theory, espoused by Mr. Vetne (Tr. 691), that any "statements" by "parties" are admissible "Admissions by Party-Opponent,"[10] (as in ordinary civil proceedings in federal district court) is not applicable in a rulemaking proceeding where participants are not "parties" and any given industry participant's conduct is not at issue, in the manner that it might be in another type of legal proceeding. The Secretary should act now, in this proceeding, to set some parameters on this type of offering.

Finally, we note our opposition to the Motion for "Supplementation" of the Record, submitted post-hearing by counsel for White-Eagle, et al.[11] We consider this Motion to be in the nature of a post-hearing brief due on this date – since that is the only post-hearing filing authorized at the close of this hearing. (Tr. 1148) Therefore, we will respond to it in the reply briefing process, as the order for post-hearing briefing would contemplate.

VIII. CONCLUSION

These proponent cooperatives respectfully request that Proposals 1, 2, 8 and 9, as modified, be adopted. The aggregate impact of adoption of these proposals should modestly

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[10] See Federal Rule of Evidence 801(d)(2).

[11] "Request for Supplementation of the Public Record of Proceedings by Dislcosure of *Ex parte* Communications (5 U.S.C. §557(d) and 7 C.F.R. §900.16)", dated April 6, 2005.

enhance the Order 33 pool, taking into account the blend price improvement which proposals 2 and 8 will provide, and allowing for the cost of Proposal 9. Moreover, the adoption of these proposals will help eliminate the current disorderly conditions in Order 33 and further the purposes of the Agricultural Marketing Agreement to establish orderly marketing conditions in fluid milk markets.

Respectfully submitted.

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